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TRADE LEGISLATION TO MARK 100TH CONGRESS

Trade continues to dominate agendas in Washington, stimulated by the record $170 billion merchandise trade deficit in 1986. Legislative action is expected this spring, and is most likely going to take form as a series of technical changes to existing trade law and export promotion programs. This month, the Administration submitted a set of proposals geared toward enhancing U.S. competitiveness through research and development incentives. Thus, trade and competitiveness have become intertwined in the same policy debate.

The FY88 appropriations process also has a variety of trade implications stemming from the allocations for export promotion and trade enforcement agencies. Needless to say, the wood industry is closely following legislative developments.

Varied Issues Must Be Addressed

The causes and circumstances of America's trade woes are complex and interrelated. They range from the macroeconomic impact of budget deficits and rates of growth in other countries, to the more focused influences of trade policies affecting specific industries. Some of the key issues:

● *Budget Deficits.* One of the underlying factors affecting the U.S. trade imbalance is the budget deficit. According to the President's Council of Economic Advisors (CEA), total public debt in 1986 amounted to $143 billion or 3.4 percent of GNP (the federal deficit plus state and local surpluses). The economy required an equivalent of 19.7 percent of GNP to meet the capital requirements generated by private domestic investment combined with this public debt.

Normally, this requirement would be met by U.S. savings, but gross private savings amounted to only 16.2 percent of GNP. The difference -- 3.5 percent -- had to be derived from other sources, i.e. foreigners (Figure 1). This is the "capital inflow" into the economy. In essence, the budget deficit causes real interest rates to rise to the point where they attract foreign capital. This at least partially explains the increased flow of imports.

Foreigners obtain capital to invest in U.S. instruments by selling their products here. If they can provide quality products at prices that appeal to U.S. consumers, they can in turn generate capital to invest in U.S. financial markets.

The CEA argues that without budget deficit reduction, or an increase in the U.S. savings rate, foreign capital will continue to be necessary and come into the United States in the form of imports.

MONTHLY STATISTICAL HIGHLIGHTS

Softwood lumber consumption reached a new high during 1986, an estimated 46.8 billion board feet.

U.S. production of softwood lumber also set a new record at 34.7 billion board feet.

The seasonally adjusted annual rate of softwood lumber production was nearly 40 billion board feet in December, 27 percent higher than December, 1985.

Wood products exports exceeded imports in December, for the first time in six years. In 1986, the value of all wood products exported was over $3 billion, up 13.5 percent from 1985.

Softwood lumber imports fell by 40 percent during the fourth quarter, bringing total softwood lumber imports in 1986 to 14.2 billion board feet, a 3 percent decline from 1985.

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●*Manufacturing Productivity.* There is a measurable difference between U.S. manufacturing productivity and productivity in other industrialized countries. In 1985, for example, output per hour in the United States rose 2.8 percent, while in West Germany it rose 6 percent and in Japan it rose 5 percent. A number of proposals have emerged which attempt to address this problem through investment and R & D incentives. The link between productivity and international competitiveness has been of somewhat greater concern in industries other than wood products, where the productivity trend in recent years has been more favorable, increasing at twice the national average.

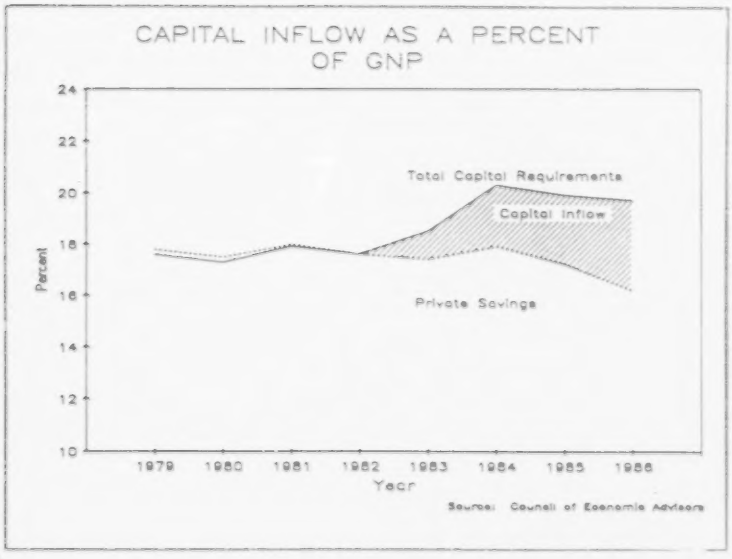
●*Exchange Rates.* Exchange rates are perhaps the most perplexing of all trade issues. Many consider the appreciation of the dollar between 1980 and 1985 to be a leading cause of America's trade deficit. A strong dollar makes U.S. exports more expensive to foreigners. The subsequent decline of the value of the dollar has not had the desired effect. There may be a lag of two years or more before its influence is felt. More likely, while the dollar has fallen *vis a vis* some currencies, it has not depreciated against currencies of other countries with which the U.S. has significant trade (Canada, Mexico, Singapore, Taiwan to name a few).

Exchange rate stability is generally regarded as a worthwhile policy objective, but difficult to implement without direct governmental interference. Secretary of Treasury Baker met this month with the economic ministers of Japan, West Germany, France, United Kingdom and Canada, to seek consensus on exchange rate intervention. The meeting produced a general agreement to maintain exchange rates at approximately current levels. West Germany and Japan also agreed to take measures to stimulate their respective economies. It is hoped that this will lead to increased purchases of U.S. goods and services.

●*International Debt.* The debt problems of many non-industrialized countries further exacerbate U.S. efforts to export. Shortages of foreign currency and mounting interest payments reduce their ability to purchase U.S. goods and services. Total external debt of developing countries exceeds $1 trillion and has been increasing every year. One of the major debtor nations is Brazil which this month placed a moratorium on debt payments.

●*Unfair Trade Practices.* Many in Congress have long been critical of the Administration's handling of unfair trade complaints. Proposals to tighten trade remedy laws and enforcement measures are almost certainly going to be part of a final legislative package, even though the Administration has been

Figure 1: Private savings have been insufficient to meet U.S. capital demand. Foreign capital — capital inflow — has been making up the slack.



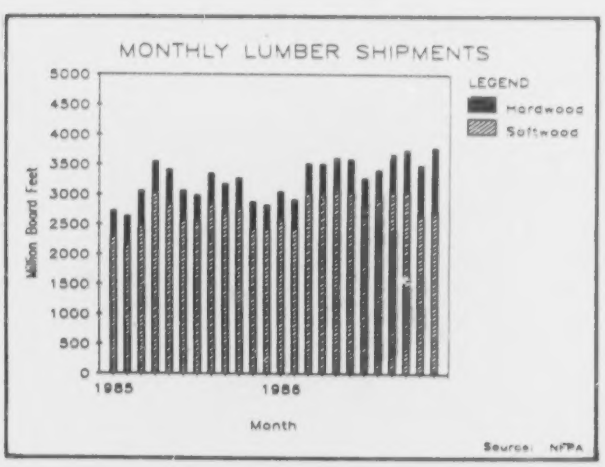
ECONOMICS MONTHLY

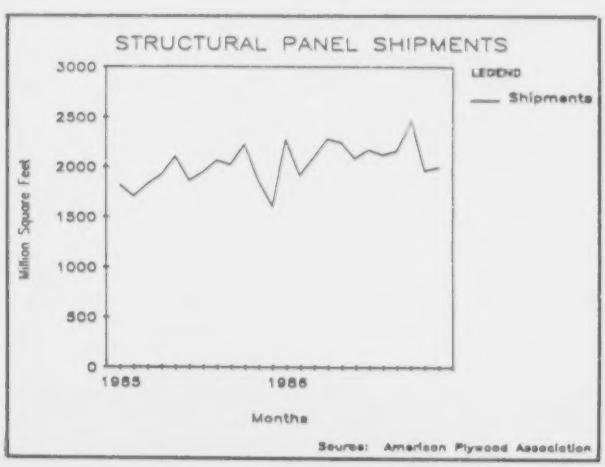
MONTHLY STATISTICAL SUPPLEMENT

Issued: February, 1987

ESTIMATED INDUSTRY TOTALS BY PRODUCING REGION

	DECEMBER 1986			DECEMBER 30, 1986	
	Production	Shipments	Orders Received	Unfilled Orders	Gross Stocks
SOFTWOOD LUMBER		(Million Board Feet)			
Southern Pine Region	833	775	765	710	2,007
Douglas Fir Region	759	783	801	668	989
Western Pine Region	864	895	828	452	1,338
California Redwood Region	146	149	149	130	395
Other Softwoods	133	133	130	258	311
TOTAL SOFTWOODS	2,735	2,735	2,673	2,218	5,040
% Change - November 1986	0.7%	3.2%	2.9%	-2.7%	0.0%
% Change - December 1985	18.7%	12.7%	9.8%	11.9%	5.8%
HARDWOOD LUMBER					
Southern Hardwood Region	170	195	165	277	824
Appalachian Hardwood Reg.	350	423	401	*	*
Other Hardwoods	368	438	401	238	685
TOTAL HARDWOODS	888	1,056	967	515	1,509
% Change - November 1986	11.3%	25.0%	4.0%	-14.7%	-10.0%
% Change - December 1985	124.8%	161.4%	152.5%	31.4%	-12.2%
TOTAL LUMBER	3,623	3,791	3,640	2,733	6,549
% Change - November 1986	3.1%	8.4%	3.2%	-5.2%	-2.5%
% Change - December 1985	34.2%	33.9%	29.2%	15.1%	1.0%
* Included in Other Hardwoods					
FLOORING		(Thousand Feet)			
Oak Flooring (Bd. Ft.)	NA	12,179	NA	7,533	7,351
Maple Flooring (Sq. Ft.)	859	793	910	3,299	1,419
STRUCTURAL PANELS (Sq. Ft.)	2,083,210	1,996,734	2,008,757	383,666	392,000
% Change - November 1986	3.1%	1.7%	17.2%	-39.5%	28.1%
% Change - December 1985	24.0%	24.4%	20.1%	-33.8%	-9.7%





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YEAR-TO-DATE INDICATORS

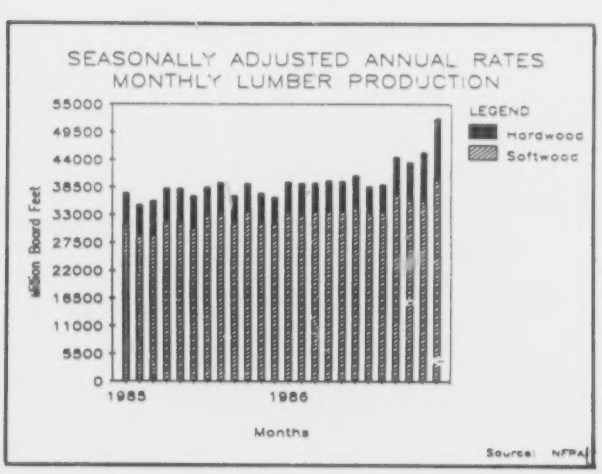
	PRODUCTION		SHIPMENTS		ORDERS RECEIVED	
	Latest Period Available	% Change	Latest Period Available	% Change	Latest Period Available	% Change
	12 mos.'86	12 mos.'85	12 mos.'86	12 mos.'85	12 mos.'86	12 mos.'85
	(Million Board Feet)					
TOTAL LUMBER	41,680	11.6%	41,615	12.4%	41,973	13.0%
TOTAL SOFTWOOD	34,725	10.9%	34,450	10.6%	34,686	11.0%
TOTAL HARDWOOD	6,955	15.3%	7,165	22.0%	7,287	24.0%
	(Million Square Feet)					
STRUCTURAL PANELS	25,978	12.1%	25,781	12.3%	25,493	11.8%

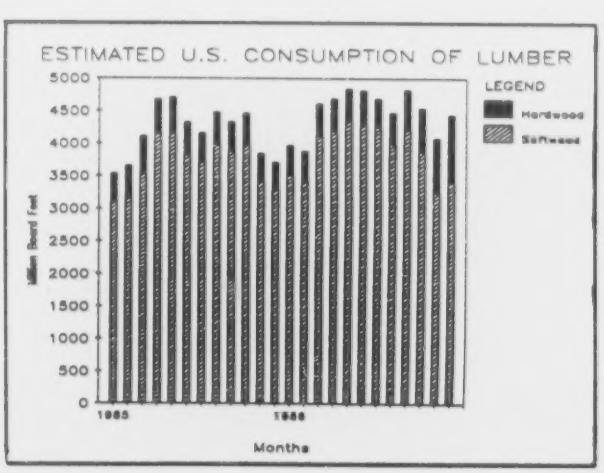
SEASONALLY ADJUSTED ANNUAL RATES

	PRODUCTION			SHIPMENTS		
		---% Change From--			---% Change From--	
LUMBER REGION	Dec. '86	Nov. '86	Dec. '85	Dec. '86	Nov. '86	Dec. '85
	(Million Board Feet)			(Million Board Feet)		
Southern Pine	11,772	2.5%	16.1%	10,843	-2.8%	3.5%
Douglas Fir	11,515	19.7%	37.7%	10,693	19.5%	19.5%
Western Pine	12,502	16.0%	25.8%	12,116	23.5%	13.3%
Calif. Redwood	2,295	1.6%	62.4%	2,001	-6.5%	11.3%
Other Softwoods	1,902	9.4%	28.8%	1,781	9.7%	13.7%
TOTAL SOFTWOODS	39,986	11.5%	27.6%	37,434	11.1%	11.8%
TOTAL HARDWOODS	12,318	27.2%	137.8%	14,397	42.5%	166.4%
TOTAL LUMBER	52,304	14.8%	43.3%	51,831	18.4%	33.3%

DOMESTIC LUMBER CONSUMPTION

	CURRENT			YEAR-TO-DATE	
	Latest Month Available	----% Change From----		Latest Period Available	% Change From
	Dec. '86	Nov. '86	Dec. '85	12 mos.'86	12 mos.'85
	(Million Board Feet)				
Total Consumption	4,330	6.0%	16.6%	53,824	7.5%
Softwood Consumption	3,291	1.2%	-0.7%	46,811	5.8%
Hardwood Consumption	1,039	24.8%	159.7%	7,013	20.2%

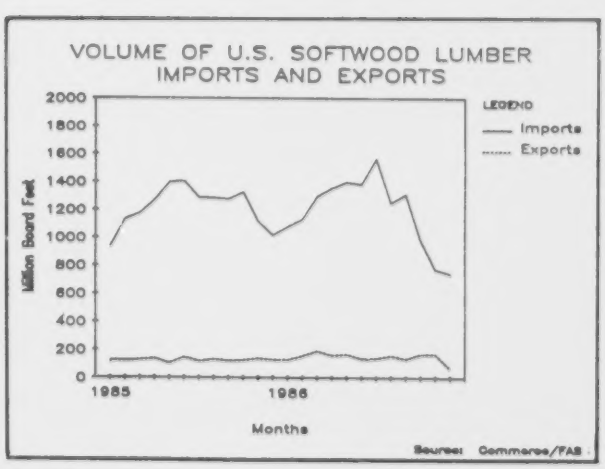


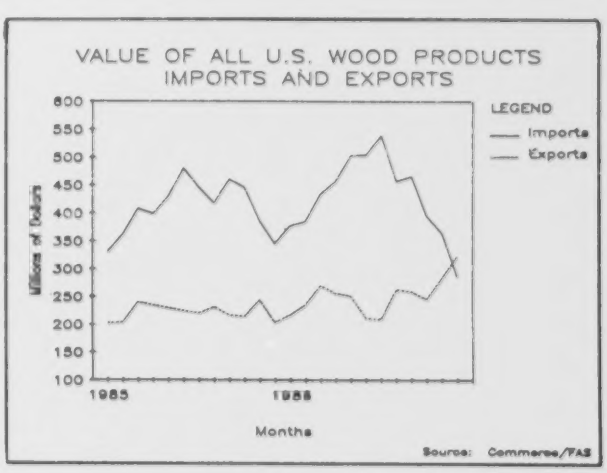


INTERNATIONAL TRADE STATISTICS

		VOLUME				VALUE			
		Dec. '86	12 mo. 1986	% Change From Nov. '86	% Change From 12 mo. 1985	Dec. '86	12 mo. 1986	% Change From Nov. '86	% Change From 12 mo. 1985
EXPORTS									
SOFTWOOD LUMBER	MMBF	183.9	1,877.0	9.5%	23.9%	68,300	643,814	10.8%	29.7%
To Canada	MMBF	26.1	360.7	-0.6%	20.7%	7,132	90,849	0.5%	22.2%
SOFTWOOD LOGS	MMBF	375.7	3,488.5	14.2%	-6.5%	121,421	1,129,370	15.3%	-3.4%
SOFTWOOD PLYWOOD	MMSF 3/8"	91.1	595.6	34.2%	85.2%	20,754	131,313	34.7%	74.6%
HARDWOOD LUMBER	MMBF	38.9	498.3	-12.8%	25.5%	25,278	337,137	-18.9%	36.2%
HARDWOOD LOGS	MMBF	9.2	138.9	-77.8%	24.9%	8,856	97,265	6.4%	6.7%
HARDWOOD VENEER	MMSFsurf	92.2	995.8	1.1%	25.6%	7,993	81,764	-3.3%	31.4%
PARTICLEBOARD	MMSF 3/4"	18.3	172.0	6.5%	44.8%	3,719	34,366	12.9%	42.2%
ALL OTHER		NA	NA	NA	NA	64,375	554,030	30.5%	15.1%
TOTAL U.S. EXPORTS		NA	NA	NA	NA	323,684	3,022,201	14.1%	13.5%
IMPORTS									
SOFTWOOD LUMBER	MMBF	739.6	14,238.2	-4.0%	-2.5%	137,234	2,961,025	-0.9%	2.4%
From Canada	MMBF	723.2	14,100.8	-5.0%	-2.8%	135,277	2,931,144	-0.8%	2.1%
SOFTWOOD LOGS	MMBF	0.3	52.1	-96.4%	-26.4%	44	7,219	-98.2%	-57.2%
SOFTWOOD PLYWOOD	MMSF 3/8"	7.7	131.6	-49.2%	50.8%	1,806	34,162	-54.3%	56.8%
HARDWOOD LUMBER	MMBF	25.8	346.9	-19.1%	-4.6%	12,819	168,297	-18.2%	-6.7%
HARDWOOD LOGS	MMBF	2.7	26.4	331.9%	-7.2%	155	4,054	-37.5%	7.4%
HARDWOOD VENEER	MMSFsurf	128.5	1,603.9	-20.0%	14.7%	10,024	114,328	-13.2%	12.3%
HARDWOOD PLYWOOD	MMSFsurf	238.5	3,805.5	-46.1%	8.1%	33,143	484,515	-42.1%	9.9%
HARDBOARD	MMSF 1/8"	51.6	855.2	-38.3%	9.3%	3,586	56,099	-30.0%	7.9%
PARTICLEBOARD	MSF 3/4"	79.2	1,133.1	-3.8%	11.1%	7,644	136,639	-35.1%	-3.6%
ALL OTHER		NA	NA	NA	NA	79,862	1,197,769	-31.7%	13.4%
TOTAL U.S. IMPORTS		NA	NA	NA	NA	286,532	5,167,441	-21.2%	5.3%

Note: Volume total is not possible because the products are in different units of measure.
Note: Particleboard imports include OSB/Waferboard.





VALUE OF NEW CONSTRUCTION

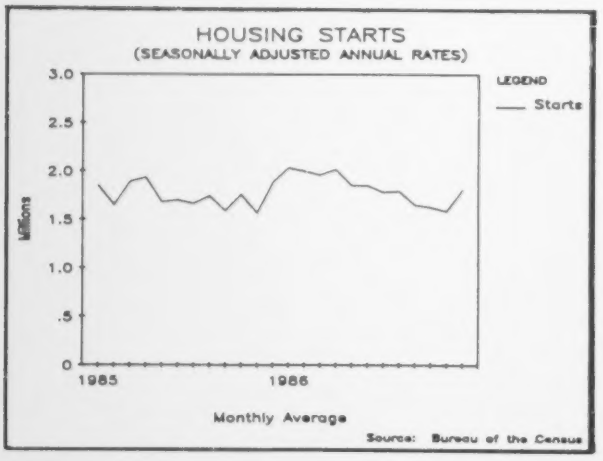
	CURRENT			YEAR-TO-DATE	
	Latest Month Available	% Change From		Latest Period Available	% Change From
	Dec. '86	Nov. '86	Dec. '85	12 mo. '86	12 mo. '85
	(Billions of Dollars)				
VALUE OF ALL NEW CONSTRUCTION PUT-IN-PLACE	28.9	-11.3%	6.0%	376.5	9.6%
Private	23.8	-10.5%	4.7%	305.4	8.8%
Residential	13.3	-14.7%	19.0%	174.3	17.4%
Nonresidential & Other	10.5	-4.5%	34.5%	131.1	2.2%
Public	5.1	-15.0%	12.6%	71.1	13.5%

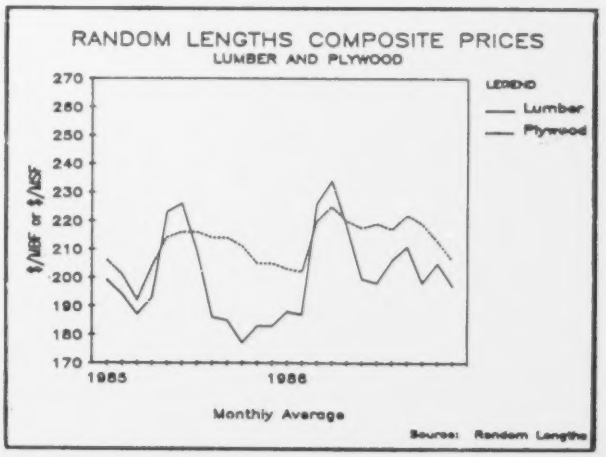
HOUSING STARTS

	Dec. '86	Nov. '86	Dec. '85	12 mo. '86	12 mo. '85
	(Thousands of Units)				
NEW HOUSING UNITS STARTED					
Total Private & Public	113.6	-2.0%	-5.7%	1,806.6	3.6%
New Private Starts	113.5	-2.0%	-5.8%	1,805.0	3.6%
Seas. Adj. Annual Rate	1,808.0	14.1%	-3.9%		
One-Family Housing Starts	72.1	-6.8%	9.2%	1,179.0	10.0%
Proportion of Total	63.5%			65.3%	
	(Number of Units)				
SHIPMENTS OF MOBILE HOMES	15,800	-8.1%	-6.5%	244,400	-13.8%

INDUSTRY EMPLOYMENT

	Dec. '86	% Change From Nov. '86	% Change From Dec. '85
	(Thousands of Employees)		
TOTAL EMPLOYMENT (Seasonally Adj.)			
All Industries	101,334	0.3%	2.3%
All Manufacturing Industries	19,190	0.2%	-1.3%
Lumber and Wood Products	749	0.9%	4.8%
Furniture and Fixtures	501	0.2%	0.4%





more significantly aggressive in enforcing countervailing duty and other remedy laws. The wood products industry was a beneficiary of two such endeavors during 1986. The shakes and shingles industry received a reprieve from import competition under a Section 201 (temporary relief from injury) decision, and the softwood lumber sector will be aided by an agreement reached between the U.S. and Canadian governments over timber subsidies.

●*Negotiating Authority.* As a matter of law, Congress must delegate authority to the president to enter into multilateral trade agreements. The president is seeking further authority through the new round of GATT discussions and the free trade talks with Canada.

●*Export Promotion.* Expansion of existing export promotion programs will be proposed as will new export oriented marketing programs at the state level. For wood products, the relevant programs include the Foreign Agriculture Service wood products marketing activities and export credit guarantees and loans to developing countries through the Commodity Credit Corporation and Export/Import Bank. The wood products industry is seeking full implementation of existing agricultural export incentives for wood products.

●*Industry Specific Relief.* Politically, the greatest pressure for trade legislation is arising out of industries severely impacted by imports, notably textiles, footwear and steel. The Congress passed, but the President vetoed, a restrictive trade bill in 1985 which would have established quotas for imports of textiles. Enactment of that law almost certainly would have led to retaliatory measures by the affected countries. That is the basic argument against protectionist legislation. It runs a high risk of backfiring, either by substituting one target country for another, or by alleviating problems in one industry while damaging the export prospects of another.

The Complex, Not the Simple

It has become apparent that the causes of America's trade problems are deep-rooted. They go beyond the simple statistics showing imports far outpacing exports to underlying economic trends intertwined with America's productivity and the federal fiscal deficit, and specific trade-related policies.

For wood products producers, the implications of trade policy are significant. Exports are one of the fastest growing markets for wood products. Protectionist efforts designed to curtail U.S. imports by imposing quotas or tariffs on certain products might result in retaliatory measures against U.S. exports, including wood products. On the other hand, credit and loan guarantee programs for less developed countries and export marketing programs have been shown to be effective vehicles for promoting wood exports.

Whatever the outcome from Congress, 1987 may turn out to be viewed as the year of trade.

THE YEAR -- 1986 -- IN REVIEW

After several tenuous years, the wood products industry experienced an "economic recovery" during 1986. Most companies finally profited from demand levels which reached new records now for three consecutive years. U.S. producers benefited from a drop in softwood lumber imports during the fourth quarter, which resulted in regaining market share and higher production.

U.S. softwood lumber production reached a record level, surpassing the previous record year of 1978. The market expanded for structural panels as well, with production and consumption also at new records. Other highlights of the year:

●U.S. softwood lumber production totaled an estimated 34.7 billion board feet. This was up 10 percent from 1985, and was 8 percent higher than in 1978. Production reached record levels in almost all regions.

●Softwood lumber consumption also set a new record for the third year in a row, finishing the year at an estimated 46.8 billion board feet.

●Imports of softwood lumber experienced the first decline in volume since 1982, and the first decline in market share since 1979. Canadian imports accounted for 30 percent of consumption in 1986, compared with 32.8 percent in 1985.

●Structural panel production reached a new high, estimated at 25.9 billion square feet for the year.

● Continued restructuring in the industry resulted in several new mergers and/or acquisitions. Among the companies which changed hands were: Hammermill Paper Company (purchased by International Paper Company), Kirby Forest Industries (purchased by Louisiana Pacific), Pacific Lumber (purchased by Maxxam Group), and S.W. Forest Industries (purchase announced by Stone Container). Other companies added new mills or acquired timberland.

●The U.S. and Canada reached an historic agreement on softwood lumber resulting in a 15 percent export tax on Canadian shipments to the U.S.

●The U.S. trade deficit also reached historic proportions, approaching $170 billion. In 1986, the U.S. merchandise trade deficit increased by 14 percent. The wood products trade deficit actually declined in 1986 by 4.5 percent over 1985. Wood products exports increased by 13.5 percent.

●Housing starts reached 1.81 million units during 1986, with 65 percent in single-family dwellings. Starts have averaged over 1.75 million units over the past four years.

●Exports of wood products were particularly strong to Europe during 1986. Structural panel exports to the European countries rose a dramatic 86 percent, and softwood lumber exports to Europe were up 24 percent. Southern pine shipments to Europe increased 35 percent.

●The Random Lengths softwood lumber composite rose to an average of $206/MBF for the year, a 6 percent increase over 1985.

●Tax law underwent a major overhaul with potentially long-lasting implications for all sectors of the economy. Forest management will continue to benefit from the deductibility of management expenses and the availability of a reforestation tax credit for qualifying landowners, but it loses the advantages of a capital gains differential which was eliminated. In general, corporations will be paying higher taxes as a result of the changes.

●The harvest on federal forests reached 11.8 billion board feet in 1986, the highest level since 1973. Since only 10.9 billion board feet was sold during the year, and 9.7 billion board feet was returned under the buyout program, the backlog of uncut volume under contract now stands at its lowest point in over 20 years.